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Supreme Court, U.S.
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No. 94-1809

IN THE

Supreme Court of the United States

OCTOBER TERM, 1995

MATSUSHITA ELECTRIC INDUSTRIAL CO., LTD. and MATSUSHITA HOLDING CORP.,

Petitioners,

vs.

LAWRENCE EPSTEIN, *et al.*,

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE PETITIONERS

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QUESTION PRESENTED

The 1990 acquisition of MCA by Matsushita gave rise to shareholder class action litigation in Delaware state court and later in a California federal district court. The named plaintiffs in each court claimed to represent the shareholders of MCA. The federal district court denied class action status and entered summary judgment for Matsushita dismissing the action.

After the dismissal of the federal action, the parties to the Delaware class action negotiated a settlement that released all claims arising out of the acquisition of MCA. The Delaware Chancery Court certified a class for settlement purposes and approved a notice informing class members of their right to opt out of or to object to the settlement. A hearing was held by the Delaware court at which objectors challenged the adequacy of the class representation and the fairness of the settlement. The Delaware court thereafter approved the settlement as fair and entered a judgment incorporating the terms of the settlement. The judgment was affirmed by the Delaware Supreme Court.

Respondents neither opted out of nor objected to the Delaware class settlement, but continued to litigate the very federal claims they had released by appealing the dismissal of the federal action to the Ninth Circuit Court of Appeals. Matsushita invoked the Delaware judgment and release as a bar to the further prosecution of the federal claims. The Ninth Circuit refused to give full faith and credit to the Delaware judgment, holding that state courts lack the power to approve a class action settlement releasing exclusively federal claims. The Ninth Circuit reversed the district court's dismissal of the federal action and entered summary judgment for plaintiffs on certain federal claims. Additionally, the Ninth Circuit directed the district court to certify a class consisting of thousands of former MCA shareholders who had elected *not* to opt out of the state court proceedings and who had accepted the proceeds of the state settlement without objection. This case presents the following question:

> Whether a federal court can withhold full faith and credit from a state court final judgment approving a class action settlement simply because the settlement included a release of exclusively federal claims.

PARTIES TO THE PROCEEDING

The named plaintiffs in the federal class action *Epstein, et al. v. MCA INC., et al.*, Docket No. 92-55675 (C.D. Cal.), are Lawrence Epstein, John Linder, Jane Rockford (as trustee of the Michael J. Rockford Trust), Maurice Karlin, Ruth Karlin, Beth Ann Karlin, and Bert P. Karlin. The plaintiff in *Minton v. MCA INC., et al.*, Docket No. 92-55632 (C.D. Cal.), is Walter Minton. These two cases were consolidated by the district court and the court of appeals and were treated as one case for purposes of the petition for a writ of certiorari. Walter Minton and Jane Rockford opted out of the Delaware settlement and are not bound by the Delaware judgment and release. Therefore, neither Walter Minton nor Jane Rockford is a respondent for purposes of this proceeding.

The defendants in the consolidated federal action were MCA, Matsushita Acquisition Corp., Matsushita Electric Industrial Co., Ltd., Matsushita Holding Corp., Lew R. Wasserman, and Sidney J. Sheinberg. The Ninth Circuit affirmed the dismissal of all claims against MCA and Messrs. Wasserman and Sheinberg, and those defendants are no longer parties. Matsushita Acquisition Corp. no longer exists by virtue of being merged into MCA.

RULE 29.1 LISTING

Pursuant to Supreme Court Rule 29.1, petitioners Matsushita Electrical Industrial Co., Ltd. and Matsushita Holding Corp. hereby state that their only parent or subsidiary that is not wholly owned is Cineplex Odeon Corp. On June 5, 1995, Matsushita sold eighty percent of its interest in MCA to The Seagram Company, Ltd.

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BRIEF FOR THE PETITIONERS

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-44a) is reported at 50 F.3d 644.[1] The findings of fact and conclusions of law of the district court (Pet. App. 45a-61a) are unreported.

JURISDICTION

The court of appeals entered its judgment on February 27, 1995 (Pet. App. 1a) and denied a timely petition for rehearing and rejected a suggestion for rehearing in banc on April 6, 1995 (Pet. App. 62a). The petition for a writ of certiorari was filed on May 3, 1995, and was granted on June 19, 1995. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

[1] References to documents contained in the Appendix to Petition for a Writ of Certiorari are designated as "Pet. App. ___." References to documents contained in the Joint Appendix are designated as "J.A. ___." References to documents contained in the record of the district court and court of appeals are designated as "R. ___."

STATUTORY PROVISION INVOLVED

Section 1738 of Title 28 provides with respect to the authenticated acts, records and judicial proceedings of any State:

> Such Acts, records and judicial proceedings, or copies thereof, so authenticated, shall have the same full faith and credit in every court within the United States and its Territories and Possessions as they have by law or usage in the courts of such State, Territory or Possession from which they are taken.

STATEMENT OF THE CASE

The Delaware Chancery Court approved an "opt out" settlement of a class action arising out of Matsushita's 1990 acquisition of MCA. The Chancery Court entered a judgment on the settlement that incorporated a release of all claims relating to the acquisition, including the exclusively federal securities law claims asserted here by respondents. The Delaware Supreme Court affirmed the judgment. The Ninth Circuit refused to give full faith and credit to the judgment on the ground that "a court's jurisdiction to extinguish claims by class *settlement* should not exceed its jurisdiction to extinguish claims by *adjudication*." *Epstein v. MCA INC.*, 50 F.3d 644, 664 (9th Cir. 1995) (reprinted at Pet. App. 1a) (emphasis added).

The Ninth Circuit decision nullified the state court judgment and freed the class members from their obligations under the court-approved contract of settlement. The Ninth Circuit thus countenanced a collateral attack on the state judgment by respondents who neither objected to nor opted out of the state court settlement. The Ninth Circuit decision undermines fundamental interests of federalism and the fostering of settlements, encourages the type of inefficient litigation strategies adopted by respondents, and forces complex class action litigations into the federal courts.

A. Matsushita's Acquisition of MCA

Matsushita purchased MCA for $6.6 billion on December 29, 1990. The acquisition involved a tender offer to the public shareholders and a privately negotiated purchase of shares

owned by MCA founder Lew Wasserman. The tender offer price of $66 cash per share gave tendering shareholders close to a 100% premium over the market price. J.A. 166. More than ninety percent of all MCA shares were tendered in response to Matsushita's offer. Pet. App. 49a.

The Wasserman transaction consisted of a tax-free exchange of Mr. Wasserman's MCA shares for an illiquid preferred stock in a Matsushita subsidiary. The preferred stock was structured to be no more valuable than the tender offer consideration. Pet. App. 13a, 50a. By design, the Wasserman transaction was entered into before the tender offer commenced and was consummated shortly after the tender offer expired. Pet. App. 48a-50a.

B. The State Court Class Actions

On September 26, 1990, the day after the *Wall Street Journal* reported that Matsushita might seek to acquire MCA, counsel for respondents and many other law firms filed complaints in the Delaware Chancery Court on behalf of a class of all MCA shareholders. These complaints and others filed thereafter were consolidated by order of the Delaware court.[2] The consolidated complaint sought injunctive relief against Matsushita's proposed acquisition of MCA. R.57, Exh. A, at 20-22.

On November 30, Matsushita issued a Schedule 14D-1 disclosing the terms of its tender offer to acquire MCA. On December 4, 1990, the Delaware plaintiffs amended the allegations of their complaint pursuant to a stipulated procedure. *See* J.A. 211. The Delaware plaintiffs added Matsushita as a defendant and alleged that (1) Matsushita and MCA were jointly responsible for misleading disclosures in the tender offer documents; (2) the MCA Board of Directors failed to maximize shareholder value because Matsushita had corrupted Mr. Wasserman and Sidney Sheinberg (MCA's chief operating officer) by offering them preferential treatment in

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[2] By order of the Chancery Court dated October 2, 1990, four law firms were designated as plaintiffs' Co-Lead Counsel, and sixteen additional firms were designated as the plaintiffs' Committee of the Whole. Counsel for respondents was named to the Committee of the Whole. J.A. 131-32.

the form of, respectively, the preferred stock and a multimillion dollar bonus, and (3) Mr. Wasserman "impermissibly negotiated preferential arrangements in connection with the transaction by which he will exchange [MCA] stock for [the preferred] stock and avoid costly capital gains taxes to which all other stockholders are subject." J.A. 217. On December 14, the Delaware plaintiffs filed a formal amended complaint elaborating on these allegations: "Matsushita willingly agreed to pay, and encouraged the payment of [the preferred stock to Mr. Wasserman and the bonus to Mr. Sheinberg] because of its expectation that this would vastly limit the independence of senior management and the MCA Board in negotiating with Matsushita and thereby save the purchaser potentially hundreds of millions or billions of dollars in acquisition costs." J.A. 147.

C. Respondents File a Federal Action That Also Purports to Represent the MCA Shareholders

On December 3, 1990, after the designation of Lead Counsel in the consolidated Delaware class action, *see* note 2, *supra*, and during the pendency of settlement negotiations in the Delaware action, *see* Pet. App. 83a, counsel for respondents filed this *Epstein* class action in a federal district court in California seeking to enjoin the Matsushita acquisition. The complaint was filed on behalf of all MCA shareholders owning stock subject to Matsushita's tender offer -- a class subsumed in the class for whose benefit the Delaware action was being prosecuted. The federal complaint, together with several subsequent related actions, alleged that the preferred stock Mr. Wasserman would receive was more valuable than the $66 per share tender offer price and that the Wasserman transaction therefore violated Securities and Exchange Commission Rule 14d-10, which requires an equal price to be paid for all stock purchases made "during [a] tender offer." *See* 17 C.F.R. § 240.14d-10. The *Epstein* complaint was later amended to assert that Matsushita also violated Rule 14d-10 by paying Mr. Sheinberg preferential consideration for his MCA shares by "ostensibly" compensating him for entering into a long-term employment contract. J.A. 91-92.

D. The First Delaware Settlement

On December 11, 1990, the parties to the consolidated Delaware action agreed to a settlement. The non-opt out settlement provided for the release of all shareholder claims arising out of the acquisition, in exchange for the payment of attorneys' fees and the modification of a "poison pill" in the charter of an MCA subsidiary that was spun off to the shareholders. J.A. 161, 165, 170-71. Notice was sent to all MCA shareholders describing the nature of the state and federal litigations, explaining that the settlement would release all claims arising out of the acquisition, including those in the *Epstein* action, and advising shareholders of their right to object to the settlement. R. 57, Exh. D.[3]

On April 22, 1991, the Delaware Chancery Court rejected the proposed settlement as inadequate. J.A. 159-71. The Chancery Court found that the state law claims asserted in the amended complaint were weak, and that the value of the settlement consideration was minimal. J.A. 165-67, 170-71. Addressing the federal securities law claims, the court noted that they had "not yet been definitively addressed" by the federal courts and therefore had "at least arguable merit." J.A. 169-70. The Chancery Court concluded "that it would be unfair to compel the release of the federal claims by approving the settlement in its present form," which did not provide class members an opportunity to opt out. J.A. 171.[4]

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[3] The only objectors to the proposed settlement were David and Andrew Minton, whose father, Walter Minton, had filed an individual complaint in the California federal district court that mirrored the allegations in the *Epstein* action (with which it was later consolidated). The basis of the Mintons' objection was twofold: (1) the settlement did not provide for opt outs, and (2) the class was not being sufficiently compensated for the release of its federal claims. Pet. App. 87a; J.A. 163, 167-68, 171.

[4] The Chancery Court also (1) noted that in reviewing a settlement a court does "not decide the merits of the issues," and (2) stated that the settlement could release federal claims:

> When a state court settlement of a class action releases all claims which arise out of the challenged transaction and is determined to be fair and to have met all due process requirements, the class

(Footnote continued)

E. The District Court Dismisses the Federal Action on the Merits

Thereafter, on February 10, 1992, the federal district court granted Matsushita's motion for summary judgment, holding that the Wasserman transaction did not violate Rule 14d-10 because stipulated facts established that the Wasserman transaction was agreed to and consummated when no tender offer was pending. Pet. App. 49a-50a, 52a-55a. The district court found tnat the preferred stock received by Mr. Wasserman was not more valuable than the $66 per share being offered to the public shareholders. Pet. App. 50a, 58a-59a. The district court also dismissed the claim challenging the payment to Mr. Sheinberg on substantive grounds. Pet. App. 51a, 59a. Respondents' appeal to the Ninth Circuit followed.

F. The Second Delaware Settlement

Subsequent to the dismissal of the federal action, and during the pendency of respondents' appeal to the Ninth Circuit, the parties to the Delaware action negotiated an opt-out settlement. The settlement provided for a payment by Matsushita of $2 million to the class in exchange for a release of all claims arising out of the MCA acquisition, including the federal securities law claims that had been dismissed in California. J.A. 187-88. By order dated October 27, 1992, the Chancery Court certified the Delaware action as a class action for purposes of settlement, and authorized the named plaintiffs and lead counsel to represent the interests of the class at the hearing which the court scheduled to consider the fairness of the settlement. J.A. 198-203.

1. The Notice to the Class

The court-approved notice of the proposed settlement mailed to each class member described the state court proceedings, the federal court proceedings, the appeal in the

> members are bound by the release or the doctrine of issue preclusion. Class members cannot subsequently relitigate the claims barred by the settlement in a federal court.

J.A. 163 (citations omitted).

Ninth Circuit, and the terms of the proposed settlement. Pet. App. 78a-94a. The Notice also:

- Advised that, if approved, the settlement would release all claims relating to Matsushita's acquisition of MCA, specifically including the securities law claims in the federal actions. *Id.* at 93a-94a.
- Informed each class member of the right to object to the settlement, *id.* at 97a-99a, and stated that any class member who failed to object would *"be deemed to have waived such objections and shall be forever barred from raising such objection in this or any other action or proceeding," id.* at 99a (emphasis added).
- Explained that class members could opt out of the settlement and that by doing so could preserve their state and federal claims. *Id.* at 96a.[5]

2. The Opt Outs and Objectors

The court-approved notice was mailed to the class members, and a summary form of notice was published in the *Wall Street Journal*. J.A. 199-200. More than 25,000 shareholders were notified. Pet. App. 69a. Only 19 members of the class exercised the right to request exclusion from the settlement. Pet. App. 69a.[6] Respondents did not opt out. Nor did

[5] In a section titled **"RIGHT TO REQUEST EXCLUSION,"** the Notice stated:

> All members of the Settlement Class have the option of excluding themselves from the Settlement Class by mailing a timely and valid Request for Exclusion . . . . By filing a valid Request for Exclusion, a member of the Settlement Class will not be precluded by the Settlement from individually seeking to pursue the claims alleged in the Delaware Actions, the California Federal Actions . . . or any other claim relating to the events at issue in the Delaware Actions.

Pet. App. 96a.

[6] Those who chose to opt-out included Walter Minton, five Minton family members and trusts, and Jane Rockford. *See* Parties to the Proceeding,

(Footnote continued)

respondents choose to object to the settlement in the Delaware Chancery Court.

The three people who did object to the settlement contended that the settlement fund was inadequate and that the settlement was the result of "collusion" between class counsel and counsel for defendants. Pet. App. 69a-70a.[7] None of the objectors asserted that the Delaware Court lacked the authority to approve a class action settlement that releases exclusively federal claims.

3. The Delaware Courts Approve the Settlement

The Chancery Court held a fairness hearing on January 21, 1993. Counsel for the objectors appeared and were heard. In its decision approving the settlement, the Chancery Court reaffirmed its prior determination that state court class action settlements can release exclusively federal claims, Pet. App. 63a, and noted that a "Court must be particularly careful in reviewing a proposed settlement that has the effect of barring claims of at least arguable merit that are not asserted in Delaware but are being asserted in another forum." Pet. App. 67a. The Chancery Court again found the state law claims of "little or no value." Pet. App. 68a. As to the federal claims, the court referenced its prior opinion, but noted that "[n]ow, however, there has been a full hearing on the federal claims and those claims have been rejected on both legal and factual grounds in the U.S. District Court." Pet. App. 68a. Acknowledging the possibility of a reversal by the Ninth Circuit, the Chancery Court observed that "the determination of the federal district court that the claims lack merit must be accorded substantial weight in determining the *present* settlement value of those claims" and concluded that the federal claims therefore had

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supra. Only 4 of the 19 opt-outs have pursued their claims individually: three Minton family members and Rockford. J.A. 182, 184.

[7] The three objectors were Walter Minton's wife (Marion Minton) and daughter (Pamela Minton) and one Mr. William Krupman, who was counseled by respondents' attorneys prior to filing his objection. J.A. 233, 248-51.

"minimal economic value." Pet. App. 68a, 69a (emphasis added).[8]

Weighing the state claims having "little or no value" and the federal claims of "minimal economic value" against the $2 million benefit to the class, the Chancery Court approved the settlement as "fair, reasonable and adequate and in the best interests of the plaintiffs and the Settlement Class." Pet. App. 74a. The court also found that the settlement was fair because "[t]he availability of the right to opt-out of the class protects the ability of class members who find the proposed settlement inadequate to continue the district court litigation." Pet. App. 69a.

The Chancery Court found that the representation of the class was adequate, that the notice to the class the "best practicable" notice, and that all the requisites of due process had been satisfied. Pet. App. 73a-74a.[9] The Chancery Court also found that the objectors "ha[d] offered no evidence of any collusion." Pet. App. 70a. The court's final judgment, entered on February 22, 1993, implemented the settlement agreement by providing for the release of all state and federal claims held by all members of the settlement class who did not opt out arising from, *inter alia*, Matsushita's tender offer, the Wasserman transaction, any of the "matters, transactions or occurrences" referred

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[8] Regarding the objectors' argument that it should await the decision of the Ninth Circuit -- which would not be rendered for another two years -- the Chancery Court observed: "If this Court rejects the settlement, the $2 million dollar benefit will vanish. . . . Unless fair settlements are promptly approved, the settlement process will be adversely impacted. Therefore, the Objectors' request that this Court indefinitely delay its review of the settlement must be denied." Pet. App. 69a.

[9] The Chancery Court found that the Delaware plaintiffs "as representatives of the Settlement Class, have fairly and adequately protected the interests of the Settlement Class and that the maintenance of this action as a class action meets all the requirements of Rule 23(a) and (b)(3) of the Court of Chancery." Pet. App. 73a-74a.

Significantly, Delaware Court of Chancery Rule 23 and Fed. R. Civ. P. 23 are virtually identical. *Cf. Grimes v. Vitalink Communications Corp.*, 17 F.3d 1553, 1555 n.2 (3d Cir.), *cert. denied*, 115 S.Ct. 480 (1994).

to in the Delaware pleadings, and all the claims asserted in respondents' federal actions. Pet. App. 74a-75a.[10]

On September 21, 1993, the Delaware Supreme Court affirmed the Chancery Court on the basis of the lower court's opinion. Pet. App. 76a.

G. The Ninth Circuit Decision

Upon the issuance of the Delaware Supreme Court affirmance, Matsushita invoked the Delaware final judgment as a bar to the continued prosecution of the appeal in the Ninth Circuit on behalf of any shareholder who had not opted out of the Delaware settlement. Matsushita relied on the Full Faith and Credit Act and this Court's decision in *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797 (1985), concerning the binding effect of an opt out class action settlement. Respondents -- who had neither opted out of nor objected to the settlement -- appeared before the Ninth Circuit and attacked the Vice

[10] The release language incorporated in the final judgment provided:

> All claims, rights and causes of action (state or federal, including but not limited to claims arising under the federal securities laws, any rules or regulations promulgated thereunder, or otherwise), whether known or unknown that are, could have been or might in the future be asserted by any of the plaintiffs or any member of the Settlement Class (other than those who have validly requested exclusion therefrom) . . . in connection with or that arise now or hereafter out of the Merger Agreement, the Tender Offer, the Distribution Agreement, the Capital Contribution Agreement [the agreement governing the Wasserman transaction], the employee compensation arrangements [the agreements governing the payment to Mr. Sheinberg] . . . this Settlement . . . or any matters, transactions or occurrences referred to in the December 4, 1990 Claim Letter and the Amended Complaint in the [Delaware] Action . . . including without limitation the claims asserted in the California Federal Actions [a defined term encompassing the *Epstein*, *Linder*, *Karlin*, and *Minton* actions, *see* Pet. App. 88a]. . . are hereby compromised, settled, released and discharged with prejudice by virtue of the proceedings herein and this Order and Final Judgment.
>
> Pet. App. 74a-75a.

Chancellor of the Delaware Chancery Court as obtuse and "passive," R. 57 at 19, 28; characterizing Delaware representatives and their counsel as corrupt, *id.* at 4, 17-18, 24, 27-28; and impugning the integrity of the Delaware state court system, *id.* at 31 ("The Delaware proceedings are little more than a sham."). Respondents also argued, for the first time, that a state court lacks the power to approve the release of "exclusively federal" claims. *Id.* at 31-34.

The Ninth Circuit denied full faith and credit to the Delaware final judgment, asserting a "policy" requiring that exclusively federal claims of a *class* be resolved by settlement only in federal court. Pet. App. 40a n.33. The court held that "a state court cannot require passive class members to contractually release their exclusively federal claims in order to enjoy the benefits of a state class action, when the court has no jurisdictional power to dispose of those claims either directly or indirectly through the doctrine of issue preclusion." Pet. App. 40a. The Ninth Circuit acknowledged that "individual plaintiffs may release whatever claims they choose in settling traditional non-class litigation," and that the same was true of derivative actions, but held that "the settlement of a class action is fundamentally different." Pet. App. 37a-38a & n.32.

With respect to the merits of respondents' federal securities claims, the Ninth Circuit held that there is an implied private right of action under Rule 14d-10, and that Rule 14d-10 covers transactions occurring not only "during [a] tender offer"-- as the Rule provides -- but also any transaction that is "an integral part" of a tender offer regardless of when it occurs. Pet. App. 17a.[11] Applying its expansive interpretation of Rule

[11] The Ninth Circuit held that every regulation promulgated under a statute that has been held to be privately enforceable automatically confers its own private right of action -- regardless of the language or purpose of the regulation. Pet. App. 5a n.8. This holding is at odds with "settled interpretive principles regarding implied causes of action," *Central Bank v. First Interstate Bank*, 114 S. Ct. 1439, 1455 (1994), and conflicts with the law of three circuits. *See Roosevelt v. E.I. Du Pont de Nemours & Co.*, 958 F.2d 416 (D.C. Cir. 1992); *Ashbrook v. Block*, 917 F.2d 918 (6th Cir.

(Footnote continued)

14d-10 to the Wasserman transaction, the Ninth Circuit concluded that, notwithstanding that the Wasserman transaction took place when no tender offer was pending, it should be deemed an integral part of the tender offer. Pet. App. 18a.[12] The court entered summary judgment for respondents and remanded for a trial to determine damages, if any. The Ninth Circuit found that the "claims of every tendering shareholder turn on identical facts and law," Pet. App. 41a, and directed the district court to certify a class consisting of *all* MCA shareholders.[13]

On May 3, 1995, Matsushita filed a petition in this Court for a writ of certiorari seeking review of the Ninth Circuit's holdings that (1) the Delaware judgment was not entitled to full faith and credit, (2) the Wasserman transaction violated Rule 14d-10, and (3) there is an implied private right of action under Rule 14d-10. This Court granted the petition with respect to the first issue.

1990); *Angelastro v. Prudential Bache Sec., Inc.*, 764 F.2d 939 (3d Cir.), *cert. denied*, 474 U.S. 935 (1985).

With respect to the merits of the Rule 14d-10 claim, the Ninth Circuit held that because the Wasserman transaction was "conditioned" on the successful completion of the public tender offer, it would be "deemed" to have taken place *during* the tender offer even though it did not in fact take place at that time. Pet. App. 17a-18a. This ruling directly conflicts with the holding in *Kahn v. Virginia Retirement System*, 13 F.3d 110 (4th Cir. 1993), *cert. denied*, 114 S. Ct. 1834 (1994), in which the Fourth Circuit recognized that Rule 14d-10 operates only during the defined period of time when a tender offer is actually taking place.

[12] Regarding the bonus payment by MCA to Mr. Sheinberg, the Ninth Circuit held that there was a genuine issue of fact whether the payment constituted "an inducement to support the tender offer and tender his own shares." Pet. App. 23a. The court vacated summary judgment for Matsushita on this claim and remanded for a determination of liability. Pet. App. 23a.

[13] Previously, the district court twice denied respondents' motions for class certification on the ground that respondents could not satisfy the elements of Federal Rule of Civil Procedure 23. *See* R. 98, 171.

SUMMARY OF THE ARGUMENT

The Delaware court approved the consensual settlement of a class action properly before it. In so doing, it exercised the established power of a court to approve a settlement of all claims arising from the controversy before it, including exclusively federal claims. Contrary to the Ninth Circuit's analysis, a class action settlement, like any other settlement, is a private contractual agreement between the parties upon which a judgment can be entered. When a state court enters a judgment upon a settlement, no legitimate federal interest is implicated that can justify intrusion by a federal court on state judicial processes. This is particularly so where, as here, the state settlement is subjected to a state court approval process that provides an opportunity for all class members who wish to pursue their claims -- state or federal -- to opt out of the settlement and do so.

I. The Ninth Circuit's decision vacated the considered judgments of a state supreme court and state trial court. The Ninth Circuit justified its interference with the finality of the state court judgment on the basis of an expressed concern for absent class members. But this Court's decision in *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797 (1985), has defined the procedural protections necessary for absent class members. When absent class members are afforded full notice of a settlement, an opportunity to be heard with respect thereto, the right to opt out, and the guardianship of the settling and appellate courts -- and ultimately this Court on direct appeal under 28 U.S.C. § 1257(a) -- no more is required, or reasonably should be. Indeed, since avoidance of duplicative litigation is an impetus for the class action mechanism, courts should *encourage* class action settlements releasing the broadest possible range of claims. The Ninth Circuit evidently distrusted the state court's evaluation of the fairness of the settlement, but such distrust has no place in our system of federalism.

II. The Delaware judgment is final and may not be undermined through collateral attack in a federal court. The Full Faith and Credit Act, 28 U.S.C. § 1738, so requires. Exceptions to the Full Faith and Credit Act are rare. This case involves

neither an express nor implied repeal of § 1738. *See, e.g., Marrese v. American Academy of Orthopaedic Surgeons*, 470 U.S. 373, 381 (1985). There is no basis for implying a congressional intent that claims under the Securities Exchange Act of 1934 may not be settled and released by agreement of private parties in state court litigation.

III. The Ninth Circuit established a novel test for determining the preclusive effect of a state court judgment entered on a class action settlement releasing federal claims. Under the Ninth Circuit's analysis, a state court can approve a class settlement only of claims that it can adjudicate. This test conflates the entirely separate concepts of release and issue preclusion and strips state courts of the power to resolve disputes properly before them.

IV. State court judgments are given preclusive effect in federal court through the Full Faith and Credit Act in order to advance the interests of federalism, comity, finality of judgments, and judicial efficiency. The costs of the Ninth Circuit's disturbance of the relationship between state and federal courts are enormously high:

- The right of parties to resolve a legal dispute by contract is undermined. When a judgment is entered on a settlement, full faith and credit has the added effect of holding parties to their bargain. The Ninth Circuit decision allows parties to renege on a court-approved contract.
- The legal system depends upon the finality of judgments. The Ninth Circuit decision eliminates finality with respect to prior state court class action settlements releasing federal claims as to which the statute of limitations has not run.
- The Ninth Circuit decision allows class members to bypass state court settlement fairness hearings, raising no objections, and then collaterally attack the state court judgment in federal court. No litigant should be permitted to intentionally sit on its arguments while a class action settlement hearing goes forward in one (state) court and then, if the judgment of that court is not to its liking, collaterally raise its objections in a second (federal) court.

- The court of appeals' decision requires parties to class action litigation to seek a federal forum because it will now be improvident for a defendant to settle a state class action involving facts that could be the basis for an exclusively federal claim. Thus, state class actions are radically discouraged, while all class action litigation that arguably contains the seed of an exclusively federal claim will be channeled into federal court.

ARGUMENT

I. A GRANT OF "EXCLUSIVELY FEDERAL" JURISDICTION TO ADJUDICATE CLAIMS DOES NOT PRECLUDE A STATE COURT FROM APPROVING A CLASS ACTION SETTLEMENT THAT INCLUDES A RELEASE OF "EXCLUSIVELY FEDERAL" CLAIMS

A court approving a settlement voluntarily reached by the parties before it does not adjudicate the rights and liabilities of the parties. Rather, the settlement agreement defines the obligations voluntarily assumed by parties. When a state court approves a settlement releasing exclusively federal claims, the court does not adjudicate those claims. *See Nottingham Partners v. Dana*, 564 A.2d 1089, 1104 (Del. 1989) ("*Dana*") ("[T]he law has uniformly distinguished between the approval of a general release and dismissal or adjudication of an exclusively federal claim. The former is within a state court's power, the latter is not."); *see also Parker v. Anderson*, 667 F.2d 1204, 1209 (5th Cir.) ("In determining the adequacy and reasonableness of the proposed settlement, the court does not adjudicate the dispute."), *cert. denied*, 459 U.S. 828 (1982); *Abramson v. Pennwood Inv. Corp.*, 392 F.2d 759, 762 (2d Cir. 1968) ("Although the state court could not adjudicate the federal claim, it was within its powers over the corporation and the parties to approve the release of that claim as a condition of settlement of the state action.").

Thus, a court need not have subject matter jurisdiction over a claim in order to approve a settlement incorporating its release. *See Grimes v. Vitalink Communications Corp.*, 17 F.3d

1553, 1564 (3d Cir.) (state courts have the power "to approve and enforce settlements which reflect the parties' intent to release all claims arising from a transaction regardless of whether the class action court has jurisdictional competency to hear those claims"), *cert. denied*, 115 S. Ct. 480 (1994); *Class Plaintiffs v. City of Seattle*, 955 F.2d 1268, 1288 (9th Cir.) ("[I]t was not necessary . . . to actually exercise subject matter jurisdiction over the claims to approve their release."), *cert. denied*, 113 S. Ct. 408 (1992); *Nottingham Partners v. Trans-Lux Corp.*, 925 F.2d 29, 34 (1st Cir. 1991) ("[A]s a matter of federal law, a state court can approve and enforce a settlement which requires a party to release claims actually brought, or potentially 'bringable,' in federal court under 'exclusive jurisdiction' federal statutes even though the state court could not adjudicate claims arising under such statutes."); *In re Corrugated Container Antitrust Litig.*, 643 F.2d 195, 221 (5th Cir. 1981) ("[E]ven when the court does not have power to adjudicate a claim, it may still 'approve release of that claim as a condition of settlement of [an] action [before it].' ") (citations omitted) (alteration in original); *Sandler Assoc. L.P. v. BellSouth Corp.*, 818 F. Supp. 695, 704 (D. Del. 1993) (The Delaware Chancery Court has the "power to approve a release encompassing federal securities law claims . . . not within the subject matter jurisdiction of the Delaware State courts."), *aff'd*, 26 F.3d 123 (3d Cir.), *cert. denied*, 115 S. Ct. 481 (1994).[14]

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[14] *See also TBK Partners, Ltd. v. Western Union Corp.*, 675 F.2d 456, 460 (2d Cir. 1982) ("[W]e have recognized the authority of a state court to approve a settlement that releases a claim within the exclusive jurisdiction of the federal courts."); *Gabelli v. Sikes Corp.*, No. 90 Civ. 4904, 1990 WL 213119, at *5 (S.D.N.Y. Dec. 14, 1990) (staying federal securities action pending court approval of Florida state court class settlement because "of the imminent possibility that the Florida courts will dispose of the exclusive federal issue by approving the settlements and its attendant releases"); *Lowenschuss v. Resorts Int'l, Inc.*, Civ. A. No. 89-1071, 1989 WL 73254, at *6, *9 n.15 (E.D. Pa. June 29, 1989) (determining that state court settlement and release bars exclusively federal claims), *aff'd without op.*, 947 F.2d 936 (3d Cir. 1991); *Seagoing Uniform Corp. v. Texaco, Inc.*, 705 F. Supp. 918, 923 (S.D.N.Y. 1989) (recognizing that release in "class

(Footnote continued)

The principal federal interest in a grant of exclusive federal jurisdiction is to achieve uniformity in *adjudications* of the rights and liabilities arising under a particular area of federal law. *See Michigan v. Long*, 463 U.S. 1032, 1041 (1983); 18 Charles A. Wright, Arthur R. Miller & E. H. Cooper, *Federal Practice and Procedure* § 4470, at 679 (1981). That federal interest is not implicated when a state court approves a settlement including a release of federal claims, because in performing that function the state court neither exercises jurisdiction over nor adjudicates the federal claims.

A settlement is ordinarily impractical unless it covers all claims, actual and potential, state and federal, arising out of the transaction at issue. A defendant would accomplish little by settling an action alleging state law claims if a federal claim arising from the same transaction could then be prosecuted on behalf of the same individuals with whom the defendant had settled. *See McDermott, Inc. v. AmClyde*, 114 S. Ct. 1461, 1467 (1994) (noting that defendants have no incentive to settle unless settlement agreement precludes possibility of further liability); *In re Nat'l Smelting, Inc.*, 722 F. Supp. 152, 178 (D.N.J. 1989) (there would be "absolutely no incentive to settle with the plaintiff [where] a settlement would be accompanied by no repose"); *Boothe v. Baker Indus., Inc.*, 262 F. Supp. 168, 174 (D. Del. 1966) (noting that it is "inconceivable" that defendant would have "surrendered" certain rights in the state settlement unless the plaintiff corporation and its stockholders "were barred once and for all from relitigating

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action derivative suit" in Delaware could foreclose Exchange Act claims); *Bernstein v. Mediobanca Banca di Credito Finanziario-Societa per Azioni*, 78 F.R.D. 1, 5 (S.D.N.Y. 1978) (finding that general release in state court derivative settlement bars federal securities derivative action). The point is indeed one of hornbook law: "Apart from claim preclusion as such, settlement of state court litigation has been held to defeat a subsequent federal action if the settlement was intended to apply to claims in exclusive federal jurisdiction as well as other claims. . . . *These rulings are surely correct.*" 18 Charles A. Wright, Arthur R. Miller & E. H. Cooper, *Federal Practice and Procedure* § 4470, at 688-89 (1981) (emphasis added).

the transactions which were the subject of" the prior proceeding); *Raskin v. Birmingham Steel Corp.*, Civ. A. No. 11365, 1990 WL 193326, at *7 (Del. Ch. Dec. 4, 1990) (stating that without "the release of federal securities law claims arising from [a] merger . . . [s]ettlement . . . would hardly be practicable").

A. The Ninth Circuit Erroneously Concluded That a Class Action Settlement Is Analytically Different From an Individual or Derivative Settlement

The Ninth Circuit's rationale for denying full faith and credit to the Delaware judgment is that an unparticularized "public policy" concern for the rights of absent class members precludes a state court from requiring "passive class members to contractually release their exclusively federal claims in order to enjoy the benefits of a state class action [settlement]." Pet. App. 40a & n.33. The court recognized that state courts have the power to approve the settlement of exclusively federal claims in an individual or derivative action, but held that the "settlement of a class action is fundamentally different from the settlement of a traditional litigation." Pet. App. 37a-38a & n.32.[15] Thus, the "policy" that motivated the Ninth Circuit is that only a federal court can approve a class action settlement that releases a federal securities law claim, even though:

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[15] Oddly, the court failed to note that derivative claims are pursued through much the same mechanism as class suits. Like class actions, derivative suits cannot be maintained or settled unless the court determines that the nominal plaintiff will "fairly and adequately represent the interests of the shareholders or members similarly situated in enforcing the right of the corporation or association." Fed. R. Civ. P. 23.1. *See In re Salomon Inc. Shareholders Derivative Litig.*, No. 91 Civ. 5500 (RPP), 1994 WL 533595, at *7 (S.D.N.Y. Sept. 30, 1994) ("[D]erivative suits, like class actions, are complex litigations of a representative nature which the Judicial Conference has determined present the necessity of close and careful court supervision to ensure in part that the interests of absent shareholders are protected.").

- a state court can determine factual issues that preclude subsequent prosecution of exclusively federal causes of action;[16] and
- non-federal and even non-judicial fora can resolve causes of action that are within the exclusive jurisdiction of the federal courts;[17] and
- a state court-approved release terminates exclusively federal causes of action in individual and derivative actions, Pet. App. 37a-38a & n.32; and

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[16] *See, e.g., Hathorn v. Lovorn*, 457 U.S. 255, 266 n.18 (1982) ("We frequently permit state courts to decide 'collaterally' issues that would be reserved for the federal courts if the cause of action arose directly under federal law."); *Becher v. Contoure Labs., Inc.*, 279 U.S. 388, 391-92 (1929) (Holmes, J.) ("That decrees validating or invalidating patents belong to the Courts of the United States does not give sacrosanctity to facts that may be conclusive upon the question in issue. A fact is not prevented from being proved in any case in which it is material, by the suggestion that if it is true an important patent is void."). Indeed, federal courts have stayed class actions alleging exclusively federal securities law claims pursuant to *Colorado River Water Conservation Dist. v. United States*, 424 U.S. 800 (1976), pending a final determination of parallel state court proceedings, on the ground that disposition of the state action might compel dismissal of the federal action. *See, e.g., Lorentzen v. Levolor Corp.*, 754 F. Supp. 987, 992 (S.D.N.Y. 1991); *Gabelli*, 1990 WL 213119, at *5.

[17] (1) Exclusively federal claims may be decided in arbitration. *See, e.g., Shearson v. MacMahon*, 482 U.S. 220, 238 (1987) (Exchange Act claims); *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 633-34 (1985) (federal antitrust claims). A judgment entered on an arbitration award resolving an exclusively federal claim is entitled to preclusive effect in a subsequent federal action. *See, e.g., Hough v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 757 F.Supp. 283, 291-92 (S.D.N.Y.), *aff'd*, 946 F.2d 883 (2d Cir. 1991). (2) State courts may adjudicate federal securities law defenses raised in response to state claims. *See, e.g., Will v. Calvert Fire Ins. Co.*, 437 U.S. 655, 658-59 (1978); *Weiner v. Shearson, Hammill & Co.*, 521 F.2d 817, 821-22 (9th Cir. 1975); *cf. Bement v. National Harrow Co.*, 186 U.S. 70, 87-88 (1902) (antitrust defenses). (3) Under principles of forum non conveniens, a foreign sovereign that has legal competence to adjudicate "somewhat similar" claims may adjudicate exclusively federal claims. *See, e.g., Lockman Foundation v. Evangelical Alliance Mission*, 930 F.2d 764, 766 (9th Cir. 1991) (holding that "Japan is the more convenient forum" to adjudicate copyright claims).

- a state court judgment can determine or resolve any non-exclusive federal cause of action (*e.g.*, a securities claim under the Securities Act of 1933).[18]

The Ninth Circuit determined that class actions are "fundamentally different" because class members "do not individually consent" to a settlement. Pet. App. 38a-39a. However, in a decision issued subsequent to *Epstein*, the Ninth Circuit rejected this reasoning, holding:

> A class action settlement, like the settlement of any other legal claim, is a "private consensual agreement negotiated between the parties". . . . The fact that it is approved by the court does not change the fact that the settlement is essentially a private, contractual agreement between the parties.

Cohen v. Resolution Trust Corp., Nos. 94-55209, 94-55218, 1995 WL 444436, at *3 (9th Cir. July 28, 1995) (citations omitted).

[18] The Ninth Circuit's decision is anomalous because it would permit state courts to approve settlements releasing 1933 Act claims, over which the state courts have concurrent jurisdiction, *see Rodriguez De Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477, 482 (1989), but not claims under the Securities Exchange Act of 1934. This ruling collides with

> the principle that the 1933 and 1934 Acts should be construed harmoniously because they "constitute interrelated components of the federal regulatory scheme governing transactions in securities." In this case, for example, petitioners' claims under the 1934 Act were subjected to arbitration, while their claim under the 1933 Act was not permitted to go to arbitration . . . . *That result makes little sense for similar claims, based on similar facts, which are supposed to arise within a single federal regulatory scheme. In addition, th[is] inconsistency . . . undermines the essential rationale for a harmonious construction of the two statutes, which is to discourage litigants from manipulating their allegations merely to cast their claims under one of the securities laws rather than another.*

Id. at 484-85 (emphasis added) (citations omitted). If, as is often the case, the same conduct or transaction gives rise to claims under both the 1933 Act and the 1934 Act, the Ninth Circuit's decision would permit a state court to approve a settlement releasing claims (asserted or unasserted) under the 1933 Act, but *not* the 1934 Act.

Here, the "private, contractual agreement" releasing the claims was negotiated on behalf of the class by class counsel acting pursuant to Delaware class action law. Thus, pursuant to Delaware Chancery Rule 23 -- which is virtually identical to Fed R. Civ. P. 23, *see* note 9, *supra* -- class members, all of whom had an opportunity to either object to or opt out of the settlement agreement, consented to the contract when it was approved by the Chancery Court upon notice to the class members. In nullifying the release that is an integral part of the settlement agreement, the Ninth Circuit ignored Delaware procedures that are designed to assure that a class action settlement is *not* "fundamentally different" from an individual settlement for purposes of preclusion analysis.

The *Epstein* court's conclusion simply cannot be reconciled with *Shutts*. In *Shutts*, this Court held that an opt-out right satisfies the requirements of due process and permits a state court class action to bind out-of-state class members who do not affirmatively consent to the state court's jurisdiction. 472 U.S. at 812-14; *see also id.* at 813 ("[T]he Constitution does not require more to protect what must be the somewhat rare species of class member who is unwilling to execute an 'opt out' form, but whose claim is nonetheless so important that he cannot be presumed to consent to being a member of the class by his failure to do so."). If, as *Shutts* holds, a class member's decision not to opt out constitutes "consent" to the jurisdiction of the state court, surely a failure to opt out of a state court class action settlement likewise constitutes effective consent to the settlement.[19] *See Eisen v. Carlisle & Jacquelin*, 417 U.S. 156, 176 (1974) (stating that class action procedure

[19] Contrary to this Court's reasoning in *Shutts*, the Ninth Circuit stated that "we would be blind to reality to think that any consent implied by class members in deciding not to opt out is comparable to the consent given by individual plaintiffs in settling their own lawsuits." Pet. App. 39a-40a. *Compare Shutts*, 472 U.S. at 811 (rejecting argument that class members must "opt in" to be bound).

was intended to "bind all class members who did not request exclusion from the suit").

As the Ninth Circuit has held elsewhere:

> [A]ll class members were given the right to opt out *after* being apprised of the terms of the settlement. Appellants were not forced into a position of having to predict whether their interests would be adequately represented. They could determine whether there had been adequate representation of their interests by reviewing the terms of the settlement. If they were dissatisfied, they could opt out of the class.

Marshall v. Holiday Magic, Inc., 550 F.2d 1173, 1177 (9th Cir. 1977). *See Thompson v. Edward D. Jones & Co.*, 992 F.2d 187, 191-92 (8th Cir. 1993); *In re Four Seasons Sec. Laws Litig.*, 502 F.2d 834, 843 (10th Cir.) (A right to opt out affords the class "the unique opportunity of judging, retrospectively, whether its interests *had been* adequately represented at a time when it was capable of excluding itself if not satisfied.") (emphasis added), *cert. denied*, 419 U.S. 1034 (1974); *Valerio v. Boise Cascade Corp.*, 80 F.R.D. 626, 640 n.9 (N.D. Cal. 1978), *aff'd and op. adopted*, 645 F.2d 699 (9th Cir.), *cert. denied*, 454 U.S. 1126 (1981).

A settlement releasing federal claims on notice and providing a right to opt out works no unwanted or unintended consequences on absent class members. Parties may be unable to predict the future issue or claim preclusive effect of an adjudication, but parties to a settlement know precisely what rights they relinquish. Thus, the members of the class participating in an opt-out settlement make a uniquely informed and voluntary choice. *See In re General Motors Corp. Pick-Up Truck Fuel Tank Prods. Liab. Litig.*, 55 F.3d 768, 792 (3d Cir. 1995) ("Since the plaintiff is offered the opportunity to opt out of the class simultaneously with the opportunity to accept or reject the settlement offer . . . *the plaintiff knows exactly what result he or she sacrifices.*") (emphasis added).

Significantly, prior decisions recognizing that a state court may approve a class settlement releasing exclusively federal

claims involved *non*-opt-out settlements. *See, e.g., Grimes*, 17 F.3d at 1555; *Nottingham*, 925 F.2d at 32; *Sandler*, 818 F. Supp. at 700. *A fortiori*, a state court class action settlement that affords opt-out rights precludes further litigation by class members who fail to opt out of the settlement.[20]

B. Outside the Ninth Circuit It Is Uniformly Held That a State Court May Approve a Class Action Settlement That Includes a Release of Exclusively Federal Claims

Prior to the Ninth Circuit's decision, state and federal case law uniformly held that a state court has authority to approve, as part of a *class settlement*, a release of exclusively federal claims arising out of the same transaction or subject matter that is the basis of the action before it. In *Nottingham,* shareholder class actions were filed first in federal court and later in Delaware Chancery Court. 925 F.2d at 30. The Delaware class representatives agreed to a non-opt out settlement providing non-monetary consideration in exchange for a global release of all state and federal claims arising out of the transactions "referred to in the complaint or the settlement documentation." *Id.* at 31. The federal plaintiffs objected to the settlement in Chancery Court and appealed that court's approval of the settlement to the Delaware Supreme Court,

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[20] Due Process is not at issue here. First, the Ninth Circuit decision is not predicated on any due process concern. Second, the questions of adequacy of representation, notice, and the provision of all requisite due process protections were litigated and decided in the Delaware Chancery Court, which held that the class representation was adequate, notice the best practicable, and the requirements of due process fully satisfied. *See* Pet. App. 73a-74a. These findings are entitled to issue preclusive effect. *See Migra v. Warren City Sch. Dist. Bd. of Educ.*, 465 U.S. 75, 81 (1984); *Nottingham*, 925 F.2d at 32. Significantly, because the Delaware action sought primarily equitable relief, no opt-out right was required. *See Grimes*, 17 F.3d at 1560 ("[T]he Delaware state court need only have provided 'notice plus an opportunity to be heard and participate in the litigation' in order to satisfy due process.") (quoting *Shutts*, 472 U.S. at 812). Since class members were afforded an opportunity both to object or opt out, the Delaware proceeding afforded *more* than adequate due process. *See Shutts*, 472 U.S. at 811-12; *Eisen*, 417 U.S. at 176.

which rejected their argument that the Chancery Court lacked the jurisdictional power to approve the release of the federal securities law claims. *Id.* (citing *Dana*, 564 A.2d at 1104-05). The federal district court thereafter found that the release validly encompassed the federal claims and granted summary judgment for defendants. The First Circuit affirmed and held:

> It is beyond cavil that a suit can be barred by the earlier settlement of another suit in either of two ways: res judicata or release. The defenses are separate and distinct. . . . The release contained in the *Dana* settlement, by its terms, met all the criteria necessary to engage the gears of the release defense for purposes of this suit: it (1) applied to appellants, (2) encompassed the claims asserted below, and (3) was legally enforceable. [Thus,] further prosecution of appellants' federal suit is foreclosed by the release defense . . . .

Id. at 31-32 (citations omitted). The First Circuit dismissed as "jejune" the contention that a state court cannot approve a class action settlement releasing exclusively federal claims:

> [A]s a matter of federal law, a state court can approve and enforce a settlement which requires a party to release claims actually brought, or potentially "bringable," in federal court under "exclusive jurisdiction" federal statutes even though the state court could not adjudicate claims arising under such statutes.

Id. at 33-34.

In *Grimes*, the Third Circuit likewise enforced a state court non-opt out class action settlement releasing exclusively federal claims pending in a federal court action brought by other members of the settlement class. Affirming the dismissal of the federal claims on the basis of a Delaware release, the Third Circuit honored the parties' intent "to settle all disputes that did or might arise out of the merger transaction" and "interpret[ed] the settlement agreement to release all potential causes of action, even those like the present claims that can only be brought in federal court." 17 F.3d at 1561 n.10. The Court observed that "[a]s a judgment, the settlement and release of claims is a contract that not only is agreed upon by the parties, but also is stamped with the imprimatur of the court with jurisdiction over the parties and the subject matter of the lawsuit." *Id.* at 1557. Like the First Circuit, the Third Circuit concluded that "as a matter of federal law a state court has the power to enter a settlement negotiated by the parties as a judgment which releases exclusive federal claims that the state court could not itself entertain." *Id.* at 1563-64; *see also* note 14, *supra,* and accompanying text.

II. THE FULL FAITH AND CREDIT ACT REQUIRED THE NINTH CIRCUIT TO GIVE EFFECT TO THE DELAWARE JUDGMENT, AND THE RELEASE IT INCORPORATES, AS REQUIRED BY DELAWARE LAW

The Full Faith and Credit Act requires federal courts to give the Delaware judgment the same effect it would be given in a Delaware state court. *See Mills v. Duryee*, 11 U.S. (7 Cranch) 481, 484-85 (1813) ("[W]e can perceive no rational interpretation of the act of congress, unless it declares a judgment conclusive when a Court of the particular state where it is rendered would pronounce the same decision."); *see also Parsons Steel Inc. v. First Alabama Bank*, 474 U.S. 518, 525-26 (1986) (reversing and remanding for determination under state preclusion rules of the effect of state court judgment on federal Bank Holding Company Act claim); *Marrese v. American Academy of Orthopaedic Surgeons*, 470 U.S. 373, 386-87 (1985) (reversing and remanding for determination under state preclusion rules of the effect of state court judgment on exclusively federal antitrust claim); *Kremer v. Chemical Constr. Corp.*, 456 U.S. 461, 481-82 (1982).

Under Delaware preclusion law -- ignored by the Ninth Circuit -- a judgment entered on a settlement bars subsequent proceedings resolved by the terms of the settlement, including exclusively federal claims. *Dana*, 564 A.2d at 1105; *In re Union Square Assocs. Sec. Litig.*, Civ. A. No. 11028, 1993 WL 220528, at *3 (Del. Ch. June 16, 1993); *Sternberg v.*

O'Neil, Civ. A. No. 8592, 1989 WL 137932, at *4 (Del. Ch. Nov. 9, 1989).[21]

"[I]n order to qualify for the full faith and credit guaranteed by federal law," the state judgment need only satisfy the minimum procedural due process requirements. *Kremer*, 456 U.S. at 481; *see also Parsons Steel*, 474 U.S. at 523; note 20, *supra*. The law of Delaware is consistent with the general rule that a judgment entered on a settlement is entitled to full effect. *See In re Union Square Assocs. Sec. Litig.*, 1993 WL 220528, at *3; *Sternberg*, 1989 WL 137932, at *4; *Schlaeppi v. Delaware Trust Co.*, 525 A.2d 562, 565 (Del. Ch. 1986), *aff'd*, 523 A.2d 981 (Del.), *cert. denied*, 484 U.S. 826 (1987); *Estrada-Izquierdo v. Aponte-Roque*, 850 F.2d 10, 13, 19 (1st Cir. 1988); *Reiter v. Universal Marion Corp.*, 299 F.2d 449, 452-53 (D.C. Cir. 1962). There is no different rule for judgments incorporating a release. *See, e.g., Nottingham*, 925 F.2d at 34; *Three Rivers Motors Co., Inc. v. Ford Motor Co.*, 522 F.2d 885, 891-92 (3d Cir. 1975). Thus, through the Full Faith and Credit Act, the release embodied in the Delaware judgment operates to bar all former MCA shareholders who did not opt out of the Delaware settlement from prosecuting the claims in this suit.

The Ninth Circuit essentially questioned the *fairness* of the Delaware court's decision. But this is precisely what the Full Faith and Credit Act prohibits. Fairness must be considered *ex ante*, not after a subsequent reversal on a point of law by an intermediate appellate court. *Cf. Federated Dep't Stores, Inc. v. Moitie*, 452 U.S. 394, 398-401 (1981). Moreover, real

[21] Delaware law provides that "[w]hen a state court settlement of a class action releases all claims which arise out of the challenged transaction and is determined to be fair and to have met all due process requirements, the class members are bound by the release or the doctrine of issue preclusion. Class members cannot subsequently relitigate the claims barred by the settlement in a federal court." *In re MCA, Inc. Shareholders Litig.*, 598 A.2d 687, 691 (Del. Ch. 1991) (citations omitted); *see also Dana*, 564 A.2d at 1104 (law "uniformly" holds that state court can release exclusively federal claims).

fairness and justice lie in holding parties to their bargains and choices, and respecting the finality of judgments. *Id.* at 401 ("This Court has long recognized that '[p]ublic policy dictates that there be an end of litigation; that those who have contested an issue shall be bound by the result of the contest, and that matters once tried shall be considered forever settled as between the parties.' ") (citations omitted).

A. The Ninth Circuit Decision Undermines Basic Principles of Federalism

The principles underlying full faith and credit are constitutional. The Framers understood that full recognition of sister state judicial proceedings was an essential component of federalism. *See Underwriters Nat'l Assurance Co. v. North Carolina Life & Accident & Health Ins. Guar. Ass'n*, 455 U.S. 691, 703-04 (1982). To encourage the sense of federation among the states, the Framers included a clause in the Constitution requiring each state to give "Full Faith and Credit . . . to the public acts, records, and judicial proceedings of every other state." U.S. Const., art. IV, § 1. James Madison argued that the Full Faith and Credit clause was indispensable to promote "harmony and proper intercourse among the States" and was "a very convenient instrument of justice." The Federalist No. 42, at 267, 271 (James Madison) (Clinton Rossiter ed., 1961).

The first Congress enacted the Full Faith and Credit Act in 1790 "specifically to insure that federal courts . . . would be bound by state judgments." *Kremer*, 456 U.S. at 483 n.24; *see also Davis v. Davis*, 305 U.S. 32, 40 (1938). The Act ensures the "comity between state and federal courts that has been recognized as a bulwark of the federal system." *Allen v. McCurry*, 449 U.S. 90, 96 (1980); *see also Growe v. Emison*, 113 S. Ct. 1075, 1082 (1993) (Full Faith and Credit Act embodies "elementary principles of federalism and comity").

Mindful of the federalist plan, this Court has consistently sought to promote:

> the notion of "comity," that is, a proper respect for state functions, a recognition of the fact that the entire

> country is made up of a Union of separate state governments, and a continuance of the belief that the National Government will fare best if the States and their institutions are left free to perform their separate functions in their separate ways. This, perhaps for lack of a better and clearer way to describe it, is referred to by many as "Our Federalism," and one familiar with the profound debates that ushered our Federal Constitution into existence is bound to respect those who remain loyal to the ideas and dreams of "Our Federalism."

Younger v. Harris, 401 U.S. 37, 44 (1971); *see also Underwriters Nat'l Assurance Co.*, 455 U.S. at 703-04 ("Ours is a union of states, each having its own judicial system capable of adjudicating the rights and responsibilities of the parties brought before it.").[22] The primary interest of the states in certain matters, including the regulation of corporate affairs of entities transacting business under state auspices, heightens the need for state court autonomy. *See CTS Corp. v. Dynamics Corp. of Am.*, 481 U.S. 69, 89 (1987) ("No principle of corporation law and practice is more firmly established than a State's authority to regulate domestic corporations.").

Recognizing that "an intrusion upon state judicial authority deeply implicates the principles of comity and may impair the smooth workings of our federal system," *Lehman v. Lycoming County Children's Servs. Agency*, 458 U.S. 502, 513 n.17 (1982), this Court historically has sought to protect state sovereignty against unwarranted federal encroachment in a broad variety of contexts:

- Holding that lower federal courts have no statutory authority to directly or indirectly review state court judgments. *See, e.g., Rooker v. Fidelity Trust Co.*, 263 U.S. 413, 416 (1923).

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[22] Congress has advanced these principles by codifying statutory limitations on federal court power to disrupt or review state court proceedings. *See, e.g.*, 28 U.S.C. § 2283 (the Anti-Injunction Act); 28 U.S.C. § 2254(b) (the statutory branch of the habeas corpus exhaustion requirement); 28 U.S.C. § 1341 (the Tax Injunction Act); 28 U.S.C. § 1342 (the Johnson Act).

- Limiting the availability of federal injunctive or declaratory relief against state civil and criminal proceedings. *See, e.g., Pennzoil Co v. Texaco, Inc.*, 481 U.S. 1, 11 n.9 (1987) (abstention doctrines "reflect a complex of considerations designed to soften the tensions inherent in a system that contemplates parallel judicial processes"); *Middlesex County Ethics Comm. v. Garden State Bar Ass'n*, 457 U.S. 423, 432-34 (1982) (state attorney disciplinary proceedings); *Juidice v. Vail*, 430 U.S. 327, 338 (1977) (state civil contempt proceedings); *Younger*, 401 U.S. at 43-44 (state criminal proceedings).

- Abstaining from the exercise of federal jurisdiction to allow state courts to function without interference. *See, e.g., Colorado River Water Conservation Dist. v. United States*, 424 U.S. 800, 817 (1976) ("'[w]ise judicial administration . . . conservation of judicial resources and comprehensive disposition of litigation'" counsel staying federal action where a related state proceeding is pending); *Burford v. Sun Oil Co.*, 319 U.S. 315, 334 (1943) ("a sound respect for the independence of state action requires the federal equity court to stay its hand").

- Requiring litigants to exhaust state remedies before seeking relief in federal court. *See, e.g., Huffman v. Pursue, Ltd.*, 420 U.S. 592, 610 (1975).

The Ninth Circuit held that "federal pre-emption" overrides the Full Faith and Credit Act and permits a federal court to deny full faith and credit to a state court judgment incorporating a class release of exclusively federal claims where "Congress has expressly denied state courts jurisdiction over an important area of federal law." Pet. App. 28a n.25. But federal preemption is not implicated by the judicial approval of a settlement. The mechanism by which the federal claims were released here is the execution by private parties of a contract which was approved by the court. *See American Airlines, Inc. v. Wolens*, 115 S. Ct. 817, 824 (1995) (courts should be reluctant to imply federal preemption that would nullify enforcement of private parties' contracts); *cf. Cohen*, 1995 WL 444436, at *3. Federal preemption is implicated

when the scope of a federal statute indicates that Congress intended to centralize *all* authority over the regulated area in the federal government. *See Building & Constr. Trades Council of the Metro. Dist. v. Associated Builders & Contractors of Mass./R.I.*, 113 S. Ct. 1190, 1194 (1993).[23]

This Court has found preemption of state court *adjudicatory* authority only in rare instances required by a congressional scheme. Thus, in *Brown v. Felsen*, 442 U.S. 127 (1979), this Court found that the grant of exclusive jurisdiction under § 17 of the former Bankruptcy Act "require[d] creditors to apply to the bankruptcy court for adjudication of certain dischargeability questions," *id.* at 129-130, because Congress had manifested an unequivocal intention "to take these § 17 claims away from state courts." *Id.* at 136. Since the Constitution vests in Congress plenary authority, exclusive of the states, to make uniform bankruptcy laws, *see* U.S. Const., art. I, § 8, cl. 4, and since Congress has established specialized bankruptcy courts to develop and apply uniform bankruptcy law, *see* 28 U.S.C. § 151, *et seq.*, giving full faith and credit to the state court judgment adjudicating dischargeability questions "would undercut Congress' intention to commit § 17 issues to the jurisdiction of the bankruptcy court." *Id.* at 135.

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[23] This Court has "never assumed lightly that Congress has derogated state regulation, but instead [has] addressed claims of pre-emption with the starting presumption that Congress does not intend to supplant state law." *New York State Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co.*, 115 S. Ct. 1671, 1676 (1995); *see CSX Transp., Inc. v. Easterwood*, 113 S. Ct. 1732, 1737 (1993) ("pre-emption will not lie unless it is 'the clear and manifest purpose of Congress'") (citation omitted); *English v. General Elec. Co.*, 496 U.S. 72, 87 (1990) ("'Undoubtedly, every subject that merits congressional legislation is, by definition, a subject of material concern. That cannot mean, however, that every federal statute ousts all related state law.'") (citation omitted). No authority has ever suggested that the Exchange Act preempts state involvement in securities regulation, and for good reason; section 28(a) of the Exchange Act expressly states that Congress did *not* intend to displace state involvement. *See* 15 U.S.C. § 78bb(a).

The factors that in *Brown* warranted a departure from standard preclusion principles have no analog in the case of a state court judgment approving a private contract of release. Congress has manifested no intent to oust state courts of their authority to approve class settlements -- and only class settlements -- in cases properly pending before them. *See* 15 U.S.C. § 78bb(a) (rights and remedies created by Exchange Act are in addition to those existing independent of the Act). No conceivable federal interest could be advanced by withholding full faith and credit from a state court judgment entered upon a class action settlement that permits class members to preserve their ability to assert federal securities law claims by opting out of the settlement. Indeed, undoing the state class action settlement would unjustifiably eviscerate the federal policy of promoting consensual resolutions of disputes.

B. The Grant to Federal Courts of Exclusive Jurisdiction to Adjudicate Exchange Act Claims Does Not Create an Implied Repeal of § 1738 for a State Court Judgment Entered on a Settlement Releasing Exclusively Federal Claims

The Ninth Circuit never undertook to determine whether the text or legislative history of the Exchange Act or Williams Act, the amendment to the Exchange Act pursuant to which Rule 14d-10 was promulgated, *see* note 25, *infra*, could support a finding of an implied repeal of the Full Faith and Credit Act for state court judgments approving opt-out class action settlements. They do not. Nor does anything inherent in an "exclusive" grant of federal jurisdiction even remotely suggest an implied repeal of the Full Faith and Credit Act in the context of a court-approved settlement releasing federal claims.

Section 1738 presumptively applies to *all* state judgments. *Marrese*, 470 U.S. at 381; *Kremer*, 456 U.S. at 468, 481-82. "[A]n exception to § 1738 will not be recognized unless a later statute contains an express or implied partial repeal." *Kremer*, 456 U.S. at 468; *see also Marrese*, 470 U.S. at 381. The Exchange Act does not expressly repeal § 1738. *See Murphy v. Gallagher*, 761 F.2d 878, 884-86 (2d Cir. 1985).

Implied repeals "are not favored." *Kremer*, 456 U.S. at 468 (quoting *Radzanower v. Touche Ross & Co.*, 426 U.S. 148, 154 (1976)). Congress is deemed aware of § 1738 and its consistent application in the courts when enacting federal laws subsequent to passage of the Full Faith and Credit Act. *See, e.g., University of Tennessee v. Elliot*, 478 U.S. 788, 796-97 (1986); *Allen*, 449 U.S. at 97-98. Thus, absent a clear indication that Congress intended a repeal of § 1738, or a "manifest incompatibility" between § 1738 and a later statute, the Court will infer that Congress did not intend to disturb the operation of § 1738. *See, e.g., Kremer*, 456 U.S. at 473 (no implied repeal unless a court finds that "Congress considered it necessary or desirable to provide an absolute right to relitigate an issue resolved by a state court").[24] This presumption imposes a "rigorous standard" for parties seeking to establish an implied repeal, and any doubts should be resolved against "overrid[ing] the historic respect that federal courts accord state court judgments." *Id.* at 471-72 & n.10; *see also Marrese*, 470 U.S. at 381 (presumption favoring § 1738 governs even "in a lawsuit involving a claim within the exclusive jurisdiction of the federal courts").

The legislative history of the Exchange Act provides no suggestion that Congress intended to create an exception to § 1738 for a state court judgment entered on a settlement releasing exclusively federal claims. *See Murphy*, 761 F.2d at 885 (Exchange Act does not impliedly repeal § 1738). Indeed, it is recognized that the creation of exclusive jurisdiction in

[24] The habeas corpus exception to the mandate of Full Faith and Credit -- the only express statutory exception to § 1738 recognized by this Court -- "finds its source in the unique purpose of habeas corpus -- to release the applicant for the writ from unlawful confinement." *Allen*, 449 U.S. at 98 n.12; *see also Sanders v. United States*, 373 U.S. 1, 8 (1963) ("Conventional notions of finality of litigation have no place where life or liberty is at stake and infringement of constitutional rights is alleged."). But even in the habeas corpus context, Congress and this Court have carefully circumscribed the scope of federal habeas corpus review in deference to the integrity of state courts and to avoid unnecessary state-federal friction. *See Coleman v. Thompson*, 501 U.S. 722, 731 (1991); *Stone v. Powell*, 428 U.S. 465, 494 n.35 (1976).

Section 27 of the Exchange Act, 15 U.S.C. § 78aa, was "pure happenstance." American Law Institute, *Study of the Division of Jurisdiction Between State and Federal Courts* 183 (1969) (calling for elimination of exclusive federal jurisdiction under the 1934 Act); *see also In re TransOcean Tender Offer Sec. Litig.*, 427 F. Supp. 1211, 1219 (N.D. Ill. 1977) (legislative history of 1934 Act is "unedifying as to the Congressional motive for vesting exclusive jurisdiction in the federal courts").[25]

This Court has consistently rejected arguments that federal statutes limit the scope of § 1738. *See Migra,* 465 U.S. at 84

[25] Early versions of the House bill failed to indicate whether jurisdiction was to be exclusive or concurrent. *See* H.R. 7852, 73rd Cong., 2d Sess., § 25 (1934). An intermediate version explicitly mandated concurrent Exchange Act jurisdiction. *See* H.R. 7924, 73rd Cong., 2d Sess., § 6(a) (1934). The bill finally reported out of the House Committee on Interstate and Foreign Commerce simply provided that "[t]he district courts of the United States . . . shall have jurisdiction of violations of this Act . . ." H.R. 9323, 73rd Cong., 2d Sess., § 26 (1934). With virtually no floor debate, the bill was amended to authorize exclusive federal jurisdiction. *See* 78 Cong. Rec. 8099 (1934); H.R. 9323, 73rd Cong., 2d Sess., § 26 (1934) (bill passed by House). The language of the Senate bill specified neither exclusive federal jurisdiction nor concurrent jurisdiction. *See* S. 3420, 73rd Cong., 2d Sess., § 26 (1934). During the debate the Senators were unable to determine the intent of the Committee on Banking and Currency. Aware of the exclusive jurisdiction language of the amended House version, the Senate decided to leave the ambiguity for the Conference Committee to resolve. 78 Cong. Rec. 8571 (1934) (remarks of Senators Steiwer, Fletcher and Byrnes). Without debate, the Conference Committee adopted the House version which became § 27 of the 1934 Act. *See* 78 Cong. Rec. 9939 (1934); S. Doc. No. 185, 73rd Cong., 2d Sess., § 23 (1934).

Congress enacted the Williams Act in 1968 as an amendment to the Exchange Act. *See Schreiber v. Burlington Northern, Inc.*, 472 U.S. 1, 12 (1985). Neither the express terms of the Williams Act nor its legislative history makes reference to the jurisdiction of the federal courts. And, this Court has recognized that the Williams Act does not preempt state regulation of tender offers. *See CTS Corp.*, 481 U.S. at 86 ("The longstanding prevalence of state regulation in this area suggests that, *if Congress had intended to pre-empt all state laws that delay the acquisition of voting control following a tender offer, it would have said so explicitly.*") (emphasis added). Thus, the Williams Act furnishes no basis for an implied repeal of § 1738 independent of the Exchange Act.

(the interplay between § 1738 and 42 U.S.C. § 1983 "embodies the view that it is more important to give full faith and credit to state court judgments than to ensure separate forums for federal and state claims");[26] *see also Marrese*, 470 U.S. at 385-86 (the force of § 1738 "certainly [is] not made less compelling because state courts lack jurisdiction over federal antitrust claims"); *Kremer*, 456 U.S. at 463, 476 (Title VII does not "supersede the principles of comity and repose embodied in § 1738"); *Allen*, 449 U.S. at 97-98 (no basis to find that the creation of a federal cause of action under § 1983 impliedly repeals the Full Faith and Credit Act).[27]

C. Respondents Were Barred from Initiating, and the Ninth Circuit Should Not Have Entertained, a Collateral Attack on the Delaware Court's Determination of Its Own Authority to Approve the Settlement

Respondents chose to stand by and not object to the settlement in the Delaware court, after receiving notice of the settlement and an opportunity to be heard.[28] These strategic

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[26] The Ninth Circuit relied on this Court's decision in *Newton v. Rumery*, 480 U.S. 386, 392 (1987), for the proposition that a release need not be enforced if the public interest in favor of settlements was outweighed by a competing federal interest. Pet. App. 40a n.33. *Newton* involved "a question important to the administration of criminal justice," namely an individual's release of potential 42 U.S.C. § 1983 claims in exchange for the dismissal of pending criminal charges. 480 U.S. at 392. This Court nevertheless *enforced* the release. *See Newton*, 480 U.S. at 394-97.

[27] The competence of the state courts to address securities law issues cannot be questioned. Every state has enacted a securities act, *see* Thomas Hazen, *The Law of Securities Regulation* 219 (1985), and a majority of states has adopted the Uniform Securities Act, which borrows much of its language and many of its standards from the federal securities laws. *See* Note, *The Securities Exchange Act and the Rule of Exclusive Federal Jurisdiction*, 89 Yale L.J. 95, 112 (1979).

[28] Respondents' counsel characterized their decision not to appear in Delaware as follows:

> We *thought* about opposing in Delaware. If we went to Delaware to oppose it what prevents defendants from offering these same lawyers a better settlement, but one we still consider inadequate. . .

(Footnote continued)

decisions bar respondents from mounting any "back door" challenge to the terms of the settlement in federal court. If respondents had objections to the authority of the Delaware courts to release federal claims, they should have raised them in the Delaware courts.[29] Having failed to raise an appropriate direct challenge to the authority of the Delaware courts, respondents are foreclosed from collaterally attacking the Delaware judgment.[30] "The need for finality within our federal

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> . . Frankly, we thought it unlikely that Vice Chancellor [now Justice] Hartnett would approve such a settlement.

R. 57 at 16 (emphasis added).

[29] By in effect overruling the Delaware courts' determinations regarding the capacity of the parties to contract, the adequacy of representation and the fairness of the settlement (and directing the certification of a federal class consisting almost entirely of MCA shareholders who had released their claims for consideration), the Ninth Circuit exercised appellate review of the final judgment of the Delaware Supreme Court in derogation of the *Rooker-Feldman* doctrine. *See Rooker*, 263 U.S. at 415 (state court's "decision, whether right or wrong, was an exercise of jurisdiction. If the [state court] decision was wrong, that did not make the judgment void, but merely left it open to reversal or modification *in an appropriate and timely appellate proceeding*") (emphasis added); *District of Columbia Court of Appeals v. Feldman*, 460 U.S. 462, 483 (1983) (lower federal courts "possess no power whatever to sit in direct review of state court decisions" and may not review any issue actually decided by a state court or any issue "inextricably intertwined with the state court's" determination).

[30] The Ninth Circuit recognized that (1) a collateral attack on a state court's determination of its own authority is not generally permitted, Pet. App. 28a n.25 (citing *Durfee v. Duke*, 375 U.S. 106, 111 (1963)), and (2) that the Delaware court had "determined that it was jurisdictionally competent to enter a judgment settling the class action." *Id.* Nevertheless, the Ninth Circuit concluded that "the policy of finality of judgments is plainly outweighed" when a state court "exercise[s] judicial power over" exclusively federal claims. *Id.* However, no federal interest is implicated when a state court approves a release of a federal claim. *See* Point I, *supra*. Moreover, this Court has confirmed that the rule that jurisdictional determinations are final applies even where the reviewing court has "exclusive jurisdiction over the subject matter of th[e] litigation." *Underwriters Nat'l Assurance Co.*, 455 U.S. at 705 n.11. While *Durfee* recognized that extraordinary circumstances might exist in which the doctrine of federal preemption would override the general rule of finality, this Court has actually recognized such an exception only in the context of

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system . . . applies with equal force to questions of jurisdiction." *Underwriters Nat'l Assurance Co.*, 455 U.S. at 706 n.13; *see Atlantic Coast Line R.R. Co. v. Brotherhood of Locomotive Eng'rs*, 398 U.S. 281, 296 (1970) (if a party to a state court proceeding "was adversely affected by the state court's decision, it was free to seek vindication of its federal right in the [state] appellate courts and ultimately, if necessary, in this Court."); *Nottingham*, 925 F.2d at 33 ("If, having objected and been overruled, appellants were still dissatisfied with the Delaware judgment, their recourse was to the United States Supreme Court by means of certiorari, not to the lower federal courts in the vain pursuit of back-door relief.").

Respondents should not be permitted to deliberately wait out the state court proceedings. "A party cannot escape the requirements of full faith and credit and res judicata by asserting its own failure to raise matters clearly within the scope of a prior proceeding." *Underwriters Nat'l Assurance Co.*, 455 U.S. at 710. As was held with similar force in *Insurance Corp. of Ireland, Ltd. v. Compagnie des Bauxites de Guinee*:

> A party that has had an *opportunity* to litigate the question of subject-matter jurisdiction may not, however, reopen that question in a collateral attack upon an adverse judgment. It has long been the rule that principles of res judicata apply to jurisdictional determinations -- both subject matter and personal.

456 U.S. 694, 702 n.9 (1982) (emphasis added) (citing *Chicot County Drainage Dist. v. Baxter State Bank*, 308 U.S. 371, 376 (1940); *Stoll v. Gottlieb*, 305 U.S. 165 (1938)).

In short, respondents were "obliged to advance [their] argument that the [Delaware] Court did not have the authority to settle [the exclusively federal claims] when it was given the opportunity to do so" in Delaware. *Underwriters Nat'l Assurance Co.*, 455 U.S. at 710. Respondents, self-styled fiduciaries, regarded the Delaware proceedings dismissively. With

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proceedings under the Bankruptcy Act and only then when a state court purported to *adjudicate* matters within the federal courts' plenary authority. *See Kalb v. Feuerstein*, 308 U.S. 433, 439 (1940).

full knowledge of their opportunity to object to or opt out of the Delaware proceedings, they chose to do neither. The consequences of that arrogant strategy cannot later be remedied on collateral attack and cannot serve as the predicate for the Ninth Circuit's erroneous and unprecedented interference with the Delaware judgment.

III. THE NINTH CIRCUIT TEST FOR DETERMINING THE PRECLUSIVE EFFECT OF A STATE COURT SETTLEMENT RELEASING FEDERAL CLAIMS IS ENTIRELY MISDIRECTED AND UNWORKABLE

The Ninth Circuit held that "a court's jurisdiction to extinguish claims by class settlement should not exceed its jurisdiction to extinguish claims by adjudication." Pet. App. 34a. Thus, under the Ninth Circuit's analysis a state court could approve the release of exclusively federal claims in individual and derivative suits, but it could not do so in class suits unless such claims "*would have been extinguished by the issue preclusive effect* of an adjudication of the state claims." Pet. App. 33a (emphasis added).

The Ninth Circuit's analysis conflates the separate concepts of release and issue preclusion. A release is the contractual relinquishment of a right by a party or its representative. Black's Law Dictionary 1289 (6th ed. 1990). A release is given legal effect under the regime of state contract law. *Digital Equip. Corp. v. Desktop Direct, Inc.*, 114 S. Ct. 1992, 2003 (1994); *Kokkonen v. Guardian Life Ins. Co. of Am.*, 114 S. Ct. 1673, 1677 (1994) ("enforcement of settlement agreement is for state courts"); *PMX Indus., Inc. v. LEP Profit Int'l*, 31 F.3d 701, 703 (8th Cir. 1994) ("A release or settlement agreement is a contract, and is construed under the legal principles applicable to the construction and interpretation of contracts."). When a release is embodied in a state court judgment it must be accorded full faith and credit. *See Grimes*, 17 F.3d at 1561-63. In contrast, issue preclusion is a judicial doctrine that bars "relitigation of issues *actually* litigated and necessary to the outcome of the first action." *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, 326 n.5 (1979)

(emphasis added) (citations omitted); *see also Marrese*, 470 U.S. at 376 n.1.

The Ninth Circuit's analysis is thus fundamentally misdirected: if what a court can *adjudicate* controls the parameters of what *the parties* can consensually decide to *release*, the defense of release will be subsumed by issue preclusion. *Nottingham*, 925 F.2d at 34 ("[u]nless the [release] defense is to be written off as some vestigial remnant of an abandoned jurisprudence -- and we think any such suggestion is fanciful" -- independent effect must be given to a release of federal claims). The invalidity of the Ninth Circuit's "jurisdictional" analysis is underscored by the court's acknowledgement that state courts have the power to approve the settlement of exclusively federal claims in individual and shareholder derivative suits. *See* Pet. App. 37a-38a & n.32. If the Supremacy Clause prohibited a state court from resolving exclusively federal claims as a matter of jurisdictional *power*, a state court plainly could not approve the settlement of exclusively federal claims in *any* context, including in individual and derivative actions.

A. The Ninth Circuit's Limitation on the Preclusive Effect of a Negotiated Release Has No Basis in Prior Law

The Ninth Circuit asserted that *National Super Spuds, Inc. v. New York Mercantile Exchange*, 660 F.2d 9 (2d Cir. 1981), and *TBK Partners, Ltd. v. Western Union Corp.*, 675 F.2d 456 (2d Cir. 1982), "together provide the doctrinal framework for using issue preclusion" to limit the authority of a state court to approve a negotiated release. Pet. App. 33a. This assertion is demonstrably wrong. *National Super Spuds* and *TBK* address the authority of class representatives, *not* the power of a state court. Moreover, these cases confirm the capacity of authorized class representatives to release on behalf of class members *any* claims that they possess in common with other class members -- even in the absence of an opt-out right. Nothing in *National Super Spuds* or *TBK* remotely suggests that issue preclusion has any bearing on -- much less restricts -- the scope of class action releases that may be negotiated by authorized representatives.

In *National Super Spuds*, a federal district court certified a class of persons who *liquidated* certain potato future contracts between April 13 and May 7, 1976. *See* 660 F.2d at 16. Thereafter, a state court class action was brought on behalf of persons who held *unliquidated* potato future contracts *after* May 7, 1976. *Id.* at 13. Although the federal class representatives "did not purport to represent members of the class or anyone else with respect to [state] claims based on unliquidated contracts," they entered into a settlement agreement and release that purported to encompass the unliquidated contracts. *Id.* at 17. The consideration paid for the release did not reflect any additional payment for the release of claims based on unliquidated contracts. *Id.* at 18. Since the settlement notice was sent to the class consisting of persons who liquidated their potato future contracts, members of the state class were unaware that approval of the federal settlement would result in the release of claims relating to the unliquidated contracts. *Id.* at 16. Enforcing a cardinal principle of due process (embodied in the commonality and typicality requirements of Fed. R. Civ. P. 23) that "named plaintiffs in a class action 'cannot represent a class of whom they are not a part,' " the Second Circuit held that the federal district court could not approve a settlement releasing claims based on unliquidated contracts because no class representative held such a claim. *Id.* at 17 (citation omitted).

National Super Spuds forbade the release of claims that "were not within the description of claims assertable by the class," *id.* at 19, as against absent members whom the named plaintiffs did not represent in connection with those claims and who received *no notice* of the proposed release. *National Super Spuds* thus demonstrates the established principle, fully applicable here, that class settlements may only discharge claims which the class representatives "possess in common with other members of the class" based upon the same set of facts. *Id.* at 16. *See also Officers for Justice v. Civil Serv. Comm'n*, 688 F.2d 615, 632 n.18 (9th Cir. 1982) ("where a particular type of relief potentially available to the class members is compromised in the settlement process, it is mainly irrelevant whether or not that relief was specifically

requested in the complaint"), *cert. denied*, 459 U.S. 1217 (1983).

In *TBK*, the Second Circuit reaffirmed the holding of *National Super Spuds* in the context of a non-opt-out settlement that released claims of class members that the court assumed it could *not* adjudicate. *TBK*, 675 F.2d at 459-60 ("in order to achieve a comprehensive settlement that would prevent relitigation of settled questions at the core of a class action, a court may permit the release of a claim based on the identical factual predicate [*i.e.*, the merger transaction at issue in both cases] as that underlying the claims in the settled class action *even though the claim was not presented and might not have been presentable in the class action*") (emphasis added); *accord National Super Spuds*, 660 F.2d at 18 n.7 ("We assume that a settlement could properly be framed so as to prevent class members from subsequently asserting claims relying on a legal theory different from that relied upon in the class action complaint but depending upon the very same set of facts"). As long as "all class members ha[ve] the same interest in maximizing the value" of the released claims, and "the settlement treats all class members identically," *TBK*, 675 F.2d at 462, the settlement is effective.[31] As *TBK* makes clear,

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[31] Adequacy of representation is not an issue in this case. Adequate representation requires that the named parties must "'be part of the class and possess the same interest and suffer the same injury' as the class members," *General Tel. Co. of the Southwest v. Falcon*, 457 U.S. 147, 156 (1982) (citation omitted), so "that the interests of the class members will be fairly and adequately protected in their absence." *Id.*, at 158 n.13. Here, the state class (all MCA shareholders as of September 25, 1990, and thereafter) included the federal class (all MCA shareholders as of November 3, 1990). And, as the Ninth Circuit acknowledged, "[t]he claims of every tendering shareholder turn on identical facts and law." Pet. App. 41a. By advancing their own interests, the named plaintiffs furthered the interests of the class: maximizing the award they could obtain regardless of legal theory. *See In re United Energy Corp. Solar Power Modules Tax Shelter Inv. Sec. Litig.*, 122 F.R.D. 251, 256 (C.D. Cal. 1988); 1 Herbert B. Newberg & Alba Conte, *Newberg on Class Actions*, § 3.13 at 3-75 (3d ed. 1992).

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National Super Spuds does *not* support "applying an issue preclusion test to limit the preclusive effect of a judgment approving a class settlement" — as the opinion below erroneously asserts. Pet. App. 31a. *National Super Spuds* rejected a class settlement that purported to extinguish certain claims that could not have been extinguished by a judgment after trial for the reason that the named plaintiffs did not possess the claims and the claims arose out of separate transactions.[32]

Adequate representation also requires that class counsel be competent to pursue the action. *General Tel.*, 457 U.S. at 157-58 n.13; *Sosna v. Iowa*, 419 U.S. 393, 403 (1975). The Delaware Chancery Court authorized the class representatives to represent all former MCA shareholders at the hearing scheduled to consider the fairness of the settlement. The professional competence of the court-appointed Delaware class counsel to prosecute a securities class action is indisputable. Court-appointed co-lead counsel for the Delaware class included two of the most preeminent shareholder litigation firms in the nation. These law firms are reported on Westlaw as having been court-approved plaintiff class representatives in scores of cases. Moreover, based on pretrial discovery in the Delaware action and their own analysis of the governing law, the co-lead counsel (and the other law firms comprising the Delaware plaintiffs' Committee of the Whole) were in a position to evaluate the merit -- and lack thereof -- of the Rule 14d-10 claim. See J.A. 273. If Delaware class counsel had concluded that the federal claims had greater value than the settlement consideration, it would have been in the interests of the class they represented, which included respondents -- as well as their own financial interest -- to reject the settlement and to assert the federal claim in federal court.

[32] The Ninth Circuit appropriated the "identical factual predicate" language of *TBK* as support for its doctrinally invalid fusion of issue preclusion and release. *TBK* employed the "identical factual predicate" inquiry only to ensure, as a matter of due process, that a commonality of interest existed among class members such that "the settlement treats all class members identically." 675 F.2d at 462. *TBK* looked to ascertain whether the "core" or "the gravamen" of the claims possessed by the class representative were "realistically identical" to those held by other class members, to insure that their interests coalesced. *Id.* at 460-61. The Second Circuit's statement in *National Super Spuds* that "[i]f a judgment after trial cannot extinguish claims not asserted in the class action complaint, a judgment approving a settlement in such action ordinarily should not be able to do so either," 660 F.2d at 18, does not support the Ninth Circuit's issue preclusion restriction on the effect of a release. As the Second Circuit made clear in *TBK*, its comment in *National Super Spuds* was

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The Ninth Circuit also mischaracterized *Grimes* and *Nottingham* by stating that those courts applied an issue preclusion test (*i.e.*, an "identical factual predicate" test) to determine the preclusive effect of a release. Pet. App. 33a.[33] But *Grimes* and *Nottingham* specifically rejected the notion that other preclusion doctrines could limit the scope of a negotiated release. *Grimes*, 17 F.3d at 1563 ("We need not address [res judicata effect of state court settlement] because the district court expressly ruled that the federal claims had been released as a part of the state court judgment"); *Nottingham*, 925 F.2d at 34 ("since the Delaware class action settlement could release federal claims over which the state court had no jurisdiction, *i.e.*, claims which would not be barred by the res judicata effect of the judgment containing the release . . . *the effect of the release was not circumscribed by the doctrine of res judicata*") (emphasis added). In accordance with the mandate of the Full Faith and Credit Act, *Grimes* and *Nottingham* properly applied Delaware preclusion principles to contractual *releases* of federal securities claims incorporated in non-opt out state court judgments *independent* of any issue preclusive effect of the state litigations.[34]

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directed at a circumstance, as in *National Super Spuds*, where a class settlement purported to extinguish claims that could not have been adjudicated by a judgment after trial because the named plaintiffs did not have the claims and the claims arose out of different facts.

[33] *Grimes* and *Nottingham* both held that issue preclusion doctrine separately precludes relitigation of facts determined by the state courts pertaining to due process, such as the adequacy of representation and the fairness of the settlement. *See Grimes*, 17 F.3d at 1562; *Nottingham*, 925 F.2d at 32.

[34] The releases in the state actions in *Grimes* and *Nottingham* extended to all matters "arising out of" specified transactions -- without referring to a specific federal complaint. The *Grimes* and *Nottingham* courts were required to analyze under Delaware preclusion principles whether the state and federal claims "arose out of the same transaction" or "shared a common gravamen" in order to ascertain whether the federal action was within the scope of the Delaware release. Here, because the Chancery Court final judgment *specifically* embodied the release of the claims asserted in respondents' action such inquiry is unnecessary. Moreover, in assessing the scope of the release in federal court, the Full Faith and

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B. The Ninth Circuit's "Issue Preclusion" Test Is Unworkable

The Ninth Circuit's issue preclusion test is not only doctrinally unsupportable, it is also unworkable, as the court's decision illustrates. The Ninth Circuit decision recognizes that the Delaware state claims included the claim that the MCA officers had "breached their fiduciary duty of loyalty by making preferential arrangements for themselves as part of the tender offer." Pet. App. 36a. The decision likewise acknowledges that "[a]t first glance" this claim "appears to be at least in the same ball park as the Rule 14d-10 claim." *Id.* The opinion then sought to escape from the issue preclusion test it had fashioned ("would have been extinguished by the issue preclusive effect of an adjudication of the settlement claims"). The escape, oddly, was that the state court would not and could not have occasion to adjudicate an issue that would also arise in the exclusively federal claim. As the court stated, "no Delaware *statutory or common law rule* . . . prohibits a shareholder from obtaining the best deal possible for himself as part of a change of corporate control," and therefore concluded that "adjudication of the claim would not have raised a question of *fact* concerning whether Wasserman or Sheinberg received preferential treatment from Matsushita." *Id.* at 36-37a (emphasis added). Thus, in the Ninth Circuit's view, in order to determine the preclusive effect of a state court class settlement, the federal court must engage in an exceedingly detailed, *post hoc* hypothetical reconstruction of how the state action would have been "adjudicated" had it not been settled.[35] As noted, however, concepts of preclusion predicated

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Credit Act required the Ninth Circuit to apply Delaware preclusion law. *See* Point II, *supra*, at 25. Delaware gives effect to a release according to its terms and recognizes a release of all state and federal claims arising from the same transaction. *See* Point II, *supra*, at 25-26. The Ninth Circuit acknowledged that the state and federal claims here arise from the same transaction. *See* Pet. App. 34a.

[35] Contrary to the Ninth Circuit analysis, Delaware law prohibits a corporate officer or director from using his position to obtain preferential treatment to the disadvantage of the shareholders in a change of corporate

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on *adjudication* are simply not germane to the effect of a *release* which, by definition, is a contractual undertaking that involves no adjudication.

The Ninth Circuit's issue preclusion test would place federal courts in the impossible position of having to determine which state claims would have been adjudicated by the state court on a *legal* basis and which on a *factual* basis (and, presumably, on which basis the hypothetical "adjudicating" state

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control. *See Citron v. Steego Corp.*, Civ. A. No. 10171, 1988 WL 94738, at *7 (Del. Ch. Sept. 9, 1988) (holding that a director-shareholder may not use "his corporate office to advantage himself in a way denied to other shareholders"); *see also Endervelt v. The Nostalgia Network, Inc.*, Civ. A. No. 11415, 1991 WL 137148, at *4 (Del. Ch. July 23, 1991) (citing *Citron*). Thus, there is no basis for the Ninth Circuit's assumption that the factual issue of preferential treatment would not have been adjudicated in state court. A factual finding of no preferential treatment would have precluded liability on the class's duty of loyalty claim. Moreover, Matsushita and the other defendants in the Delaware action were fully prepared to argue, in defense of the state fiduciary duty claim, not only that as a legal matter an insider may bargain for a preference for his or her shares not available to the public as long as the sale does not disadvantage other shareholders, but also that the Wasserman preferred stock was not more valuable than the public tender offer price. Had defendants in the Delaware action prevailed on the valuation issue, that determination would preclude the recovery of damages under the federal Rule 14d-10 claim. Similarly, the Delaware non-disclosure claims alleging, *inter alia*, a failure to disclose that Mr. Wasserman purportedly received consideration more valuable than the tender offer price would necessarily have entailed proof of the predicate fact of higher value, an issue that is central to respondents' Rule 14d-10 claim. Finally, the defendants in Delaware were prepared to demonstrate that the Sheinberg payment was not in consideration for his MCA shares -- a conclusion that would negate any Rule 14d-10 claim based on that payment. Thus, the core factual predicate underlying the state claims embodies essential elements of the federal claims. As pleaded and released, the state claims depended on, *inter alia*, whether "the [acquisition] also provides for substantial payments and other benefits for [Wasserman and Sheinberg] that will not be shared by MCA's public stockholders," specifically including Mr. Wasserman's receipt of preferred stock. J.A. 145. Accordingly, even under the Ninth Circuit's own test, the factual predicate of the state claims encompasses predicate facts necessary to support the federal claims and would thus lead to issue preclusion in the federal court had they been adjudicated.

court would have ruled upon a claim challenged on *both* grounds). The federal court would be required to undertake this inquiry regardless of the stage at which the state action was settled, even if no discovery had occurred to develop and test the allegations of the complaint. Under this test, the preclusive effect of a state court settlement would then depend on the outcome of some federal court's resolution of these hypotheticals. The decision thus injects a vast element of uncertainty and intricacy into the previously straightforward task of measuring the preclusive effect of state court class settlements.

The Ninth Circuit's issue preclusion analysis of a negotiated release thus operates to defeat the expectations and intentions of the parties to a consensual settlement. One of the chief advantages of a volitional settlement is that it permits the parties to define their rights precisely, and eliminate as completely as the negotiated language they employ permits, any unintended consequences that may follow adjudications, such as the uncertain issue preclusive effect of an adjudication in subsequent proceedings. By introducing the uncertainties surrounding the preclusive effect of an adjudication into a negotiated settlement, the Ninth Circuit's decision directly interferes with the ability of settling parties to determine conclusively the meaning of their agreement and embody that meaning in a court-approved settlement.

IV. THE NINTH CIRCUIT'S DECISION DISCOURAGES COMPREHENSIVE CLASS ACTION SETTLEMENTS, UNDERMINES THE FINALITY OF JUDGMENTS, PERMITS PARTIES TO ABROGATE THEIR SETTLEMENT CONTRACTS, AND PROMOTES UNNECESSARY LITIGATION IN THE FEDERAL COURTS

In addition to advancing comity, the recognition of state court judgments approving class action settlements promotes consensual resolution of complex litigation, advances finality interests, holds litigants to the bargains they voluntarily make, conserves federal judicial resources and discourages duplicative and vexatious litigation. The Ninth Circuit's decision undermines each of these objectives.

A. Encouraging Settlements

Federal courts should facilitate -- not undermine -- the settlement of litigation. *See, e.g.*, *McDermott*, 114 S. Ct. at 1467-69 (adopting proportionate share approach to judgment reduction because, *inter alia*, it promotes "public policy [that] wisely encourages settlements" and unitary disposition of litigation). There is no reason to believe that class action settlements reached under the supervision of state courts are in any respect less important, less reasonable or less fair than those reached under federal supervision. The Ninth Circuit's decision, however, assures that there will be fewer state court class action settlements. Simply stated, the Ninth Circuit decision prevents parties to a state class action from achieving a comprehensive settlement whenever the transactions and events at issue might also form the basis for an exclusively federal claim.[36]

Settlements are an important mechanism for resolving "mass litigation." *See, e.g.*, *In re General Motors Corp.*, 55 F.3d at 778, 784 ("[I]ncreased use of settlement classes has proven extremely valuable for disposing of major and complex national and international class actions in a variety of substantive areas ranging from toxic torts (Agent Orange) and medical devices (Dalkon Shield, breast implant), to antitrust cases (the beef or cardboard container industries) . . . . Courts

[36] The decision below will affect a wide variety of cases in which facts underlying state law claims may also form the basis of exclusively federal claims, such as Admiralty, 28 U.S.C. § 1333; Antitrust, 15 U.S.C. § 1; Commodity Exchanges, 7 U.S.C. § 25(c); CERCLA, 42 U.S.C. § 9613(b); Patent and Copyright, 28 U.S.C. § 1338; Securities, 15 U.S.C. § 78aa; and Single Employer Plans Under ERISA, 29 U.S.C. § 1370 (West Supp. 1995). *See, e.g.*, *Minnesota v. Mid-Minn. Associated Physicians*, No. C7-91-558, 1991 WL 340170, at *3 (Minn. Dist. Ct. July 2, 1991) (consent judgment releasing, *inter alia*, federal antitrust claims); *Texas v. Coca-Cola Bottling Co. of the Southwest*, No. 84C1-15586, 1986 WL 22186, at *3 (Tex. Dist. Ct. July 1, 1986) (final judgment releasing, *inter alia*, federal antitrust claims); *Delaware v. Mid-Atlantic Paving Co.*, Civ. A. No. 7197, 1983 WL 14930, at *2 (Del. Ch. June 24, 1983) (final judgment and consent decree releasing, *inter alia*, federal antitrust claims).

should favor the use of devices that tend to foster negotiated solutions to these actions"); *cf. Malcolm v. National Gypsum Co.*, 995 F.2d 346, 348 (2d Cir. 1993) ("One of the greatest challenges facing both state and federal courts is the crush of tort suits arising from the extensive use of asbestos . . . throughout much of this century"); *see generally Mattoon v. City of Norman*, 633 P.2d 735, 737 (Okla. 1981) (class actions assumed additional importance "when it became apparent that judicial efficiency in meeting present-day litigation explosion demanded that, as far as possible, multiple suits arising from the same facts and involving like questions of law be reduced in number or eliminated").[37]

B. Honoring the Right of Parties to Contract

Defendants are entitled to rely on the binding effect of a negotiated release. *See Dacanay v. Mendoza*, 573 F.2d 1075, 1078 (9th Cir. 1978) ("a litigant can no more repudiate a compromise agreement than he could disown any other binding contractual relationship"); *cf. PMX Indus.*, 31 F.3d at 703 (8th Cir. 1994) (holding that parties are bound to the broad terms of an unambiguous release, regardless of subjective intent). This reliance interest is destroyed if class members are permitted to accept the benefit of a settlement and renege on their promise not to sue. The Ninth Circuit's decision intruded upon the parties' consummated and court-approved agreement, and vitiated an integral part of the bargained-for consideration to be received by Matsushita.

[37] *See Air Line Stewards & Stewardesses Ass'n v. Trans World Airlines, Inc.*, 630 F.2d 1164, 1167 (7th Cir. 1980) (the preference for settlement "has particular force regarding class action lawsuits"), *aff'd*, 455 U.S. 385 (1982); *In re United States Oil & Gas Litig.*, 967 F.2d 489, 493 (11th Cir. 1992) ("Public policy strongly favors the pretrial settlement of class action lawsuits.") (citation omitted); *Armstrong v. Board of Sch. Directors*, 616 F.2d 305, 313 (7th Cir. 1980) ("there is an overriding public interest in favor of settlements"); *Georgine v. Amchem Prods., Inc.*, 157 F.R.D. 246, 338 (E.D. Pa.) (approving mass asbestos settlement), *app. docketed*, 94-1927 (3d Cir. 1994); 2 *Newberg on Class Actions* § 11.41 at 11-85.

This Court has enforced in a variety of contexts the principle that litigants must be bound by the litigation judgments that they make. *See, e.g.*, *McDermott*, 114 S. Ct. at 1471 (adopting proportionate share method of judgment reduction after partial settlement because the plaintiff's recovery had been limited "not by outside forces but by its own agreement to settle"); *Moitie*, 452 U.S. at 401-02 (parties should be held to their "free, calculated, deliberate choice not to appeal") (quotations omitted). The Ninth Circuit's decision defeats the intent of the parties in entering into the Delaware settlement and allows litigants to break their contractual commitments with impunity. *See, e.g., Thompson.*, 992 F.2d at 191 n.5. ("To the extent that the preclusion of 'all claims of any nature whatsoever' is an integral part of the settlement bargain entered into for [defendant] and the class representatives, this Court cannot now modify the terms of that bargain at the insistence of one class member."); *Bear v. Nix*, 977 F.2d 1291, 1295 (8th Cir. 1992); *Ruskay v. Waddell*, 552 F.2d 392, 398 (2d Cir.) ("One who gives a general release has had his opportunity to press his claim . . . . Once the decision to settle is made, a party must abide by it."), *cert. denied*, 434 U.S. 911 (1977).

C. Preserving the Finality of Judgments

The public policy favoring finality of judgments entered on class action settlements is at least as strong as the policy regarding the finality of judgments entered on a trial verdict. As a matter of immediate concern, the Ninth Circuit decision retroactively threatens the finality and repose of any fully consummated state class action settlement that released claims which the court approving the settlement did not have jurisdiction to adjudicate and which are not time-barred. *Cf. McCleskey v. Zant*, 499 U.S. 467, 493 (1991) (noting "the law's interest in finality"); 1B J. Moore, J. Lucas & T. Currier, *Federal Practice*, ¶ 0.405[2], at 189-90 (2d ed. 1984) (underlying policy of preclusion "is the objective of judicial finality").

The Ninth Circuit decision also opens the door to manipulation by class members who, as in this case, can obtain a settlement in state court and thereafter litigate in federal court. This threat is not confined to the securities field; the Ninth Circuit

invites collateral attacks on any case in which the state class releases claims within the exclusive jurisdiction of the federal courts, such as claims arising under the antitrust, patent, and environmental laws. *See* note 36, *supra*.

D. Minimizing Unnecessary Litigation in the Federal Courts

The Ninth Circuit's decision will increase class action litigation in the lower federal courts. Defendants will be uninterested in negotiating incomplete releases in state cases. Class action plaintiffs will, in turn, be required to file any colorable federal claim in federal court so that global disposition of cases may be achieved. Federal courts thus will become the forum for litigation traditionally handled by state courts, even when the core of the parties' dispute centers on such traditional state law claims as breach of directors' fiduciary duties. *See McCarren v. Town of Springfield*, 464 U.S. 942, 944 (1983) ("At a time when judges and observers are increasingly concerned with the work load of the federal courts, the application of principles of res judicata to disputes such as this might both conserve the time of the federal courts and make for a more orderly resolution of this and similar disputes.") (Rehnquist, J., dissenting from denial of certiorari).

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In sum, Matsushita negotiated a consensual settlement of the Delaware action, paid money for a comprehensive release, assumed the risk that shareholders might opt out and continue to prosecute their claims, and participated in a process in which the settlement was subjected to a fairness review by the Chancery Court and the Supreme Court of Delaware. In denying full faith and credit to the judgment entered upon the Delaware settlement, the Ninth Circuit announced a new rule which radically and improvidently redefines the relationship between state and federal courts. As stated in *Sandler Associates*:

> [T]he state court-approved release forecloses this federal action based on principles of comity between state and federal courts. To deny effect to a release of claims merely because it was given in an action commenced in state court would invite unprecedented consequences.

> Such a doctrine would unjustifiably proliferate litigation, defeat legitimate expectations of settling parties, engender uncertainty among class members and defendants as to their ability to retain the benefit of settlements, discourage settlements altogether and create unwarranted conflict between state and federal courts.

818 F. Supp. at 705.

CONCLUSION

For all of the foregoing reasons, the judgment of the Ninth Circuit Court of Appeals should be reversed. The case should be remanded with instructions to dismiss the complaints with prejudice as to those plaintiffs who failed to opt out of the Delaware settlement.

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Respectfully submitted,

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